

Generally, sales of "canned" computer software are taxable retail sales in Illinois. See 86 Ill. Adm. Code 130.1935. (This is a GIL).

March 29, 1999

Dear Xxxxx:

This letter is in response to your letter dated February 24, 1999. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

Thank you for our phone conversation last week and for your offer to answer questions related to our obligation to collect and turn over to the state of Illinois sales taxes on our transactions.

We are an Illinois corporation whose primary business is computer software consulting. We will soon begin a new, but related, business: licensing software to engineering firms and individual engineers. The items in question are produced in another country. We intend to take orders from these engineers, customize the software to meet their specific requirements, and provide them with the disks under license.

Are these transactions subject to the Illinois sales tax when the recipient is located in this state? If so, what is the appropriate tax rate, and will it depend on where the customer is located? Our business is in CITY.

Your prompt response will be sincerely appreciated. Thank you.

Generally, sales of "canned" computer software are taxable retail sales in Illinois. See the enclosed copy of 86 Ill. Adm. Code 130.1935. However, if the computer software consists of custom computer programs, then the sales of such software may not be taxable retail sales. See Section 130.1935(c).

Custom computer programs or software are prepared to the special order of the customer. The selection of pre-written or canned programs assembled by vendors into software packages does not constitute custom software unless real and substantial changes are made to the programs or creation of program interfacing logic. See Section 130.1935(c)(3).

If transactions for the licensing of computer software meet all of the criteria provided in Section 130.1935(a)(1), neither the transfer of the software or the subsequent software updates will be subject to Retailers' Occupation Tax.

A license of software is not a taxable retail sale if:

- A) it is evidenced by a written agreement signed by the licensor and the customer;
- B) it restricts the customer's duplication and use of the software;
- C) it prohibits the customer from licensing, sublicensing or transferring the software to a third party (except to a related party);
- D) the vendor will provide another copy at minimal or no charge if the customer loses or damages the software; and
- E) the customer must destroy or return all copies of the software to the vendor at the end of the license period.

As stated above, licenses of computer software are not taxable if they meet all of the criteria listed in Section 130.1935(a)(1). However, item (D) of that part requires the license to contain a provision requiring the vendor to provide another copy at minimal or no charge if the customer loses or damages the software. The Department has deemed software license agreements to have met this criteria if the agreements do not contain a provision about the loss or damage of the software, but the vendors' records reflect that they have a policy of providing copies of software at minimal or no cost if the customers lose or destroy the software.

Item (E) of this part also requires a license to require a customer to destroy or return all copies of the software to the vendor at the end of the license period. The Department has also deemed perpetual license agreements to qualify for this criteria even though no provision is included in the agreements that requires the return or the destruction of the software.

For your information, we have enclosed a copy of 86 Ill. Adm. Code 270.115 which is the regulation regarding Jurisdictional Questions related to the Home Rule Municipal Retailers' Occupation Tax. As you will note, it is the Department's opinion that the sellers' acceptance of the purchase orders or other contracting action in the making of the sales contract is the most important single factor in the occupation of selling. If purchase orders are accepted at the sellers' place of business within the municipality, the sale is at retail, and the purchasers receive physical possession of the property in Illinois, the sellers incur Home Rule Municipal Retailers' Occupation Tax liability in that home rule municipality.

If purchase orders are accepted outside this State, but the tangible personal property which is sold is in an inventory of the retailers located within a Home Rule municipality at the time of its sale, or is subsequently produced in the Home Rule municipality, then delivered to the purchasers in Illinois, the place where the property was located at the time of the sale, or at the time it was subsequently produced, will determine where the seller is engaged in business for Home Rule Municipal Retailers' Occupation Tax purposes regarding

that sale.

When the purchase orders are not accepted in Illinois, nor is the property located in Illinois at the time of the sale or when it is subsequently produced, the transactions will not be subject to Home Rule tax. The transactions will, however, be subject to Illinois Use Tax, which sellers having a physical presence in this State must collect and remit.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.